

February 3, 2005

Mr. Gary M. Jackson
Assistant Administrator for Size Standards
409 Third Street, SW
Washington, DC 20416

Re: RIN 3245-AF22 – “SBIR Size Standards for Venture Capital Companies”.

Dear Mr. Jackson:

As a small business specializing in research and development (R&D) in advanced laser and precision magnet devices and systems, we are opposed to any proposed changes in the Small Business Innovation Research (SBIR) program that will allow large firms access to these SBIR funds through indirect ownership of small businesses via venture capital (VC) companies. We are also opposed to any small companies with controlling interests by large VC companies, as defined by SBA standards, from being allowed to participate in the SBIR program. Many large corporations already either operate their own venture capital companies or are partners in these companies. These VC companies then acquire or have controlling interest over small business technology companies that are eligible for federal R&D funds through the SBIR program. These small businesses have access to funds from the VC company. Such funds are not available to small businesses that are not supported by VC funding and, hence, this places these “true” small businesses at an unfair disadvantage. A major reason for the SBIR program is to help small businesses compete against the “deep pockets” of the large corporations. The proposed changes to the SBIR program defeats this goal.

Our company has won and successfully completed several Phase I and II SBIR grants. These grants have been critical in developing our company’s new technology. As an example, through a Department of Energy SBIR grant we developed new types of tunable magnet devices for electron beam accelerators, which use permanent magnets rather than electromagnets. Our patented device is unique because it allows us to remotely change the magnetic field even though we are using permanent magnets.

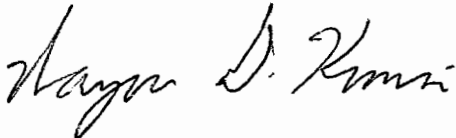
We know from first-hand experience working as a subcontractor to large companies, such as Boeing and Northrop-Grumman, that it is extremely difficult competing with these companies in the development of new technology. If large corporations and/or large VC firms are allowed to siphon money from the SBIR program through the “backdoor,” then it will have the following detrimental effects.

- 1) Because these VC-funded small businesses have access to non-SBIR funds, this will allow them to use these funds to perform preliminary work in support of their SBIR proposal and to help prepare their proposal. This gives their proposal an unfair advantage over other small businesses that cannot afford to spend such funds to enhance their proposals.
- 2) The SBIR share of the total federal R&D budget is only 2½ percent. Allowing VC-funded small businesses to participate in the SBIR program further reduces the scarce funds available to give to other small businesses. As it is, many worthy SBIR proposals are not granted simply because of lack of funds. Hence, permitting VC-funded companies to submit SBIR proposals will enlarge the pool of participants and worsen an already bad situation.
- 3) One might argue that any small business has access to VC funding and, therefore, should not be discriminated against with regard to the SBIR program. In reality, VC funding is not appropriate and/or not available for many small businesses, especially those in cutting-edge technologies where the commercial applications may be less clear or are too far in the future to interest any VC firm. It is precisely these types of companies that vitally need access to the SBIR funds because their risks are too high or uncertain even for a VC firm.
- 4) From a more fundamental viewpoint, the SBIR program is intended to help small businesses that, by definition, do not have access to substantial financial resources. VC companies, even without the involvement of large corporations, already have access to billions of dollars of funds. VC companies would love to have their small businesses win SBIR grants because it leverages the VC funds. Allowing VC-funded small businesses in the SBIR program will undoubtedly lead to accusations that federal monies are being used to subsidize big business. And, these accusations would be true!
- 5) The major interest of VC companies is to achieve a return on investment (ROI) in a relatively short time frame and for as low a risk as feasible. Hence, this will naturally favor supporting primarily low-risk projects that can be quickly brought to market. This business model is fine for large companies or for small businesses supported by VC firms, but it is counter to the fundamental purpose of the SBIR program. This purpose is to encourage innovative R&D, which often is high-risk and requires a long time to develop.
- 6) For the preceding reasons, we believe the profile of successful SBIR companies will become skewed towards those companies that have VC support. As mentioned, a VC-backed small business has more money to prepare a better SBIR proposal. They can more easily afford to perform preliminary work to enhance their SBIR proposal. Small businesses that do not have VC funding will be forced to look for VC funding in order to compete, but they will more often than not fail because the VC companies are not interested in high-risk, low ROI projects.

- 7) The availability of money outside the SBIR program directly impacts the probability of winning multiple SBIR grants. Outside money helps increase the probability of winning a Phase I grant. Outside money can be used during the Phase I program to help ensure the Phase I program is successful. This then helps increase the probability that the Phase II proposal will be granted. While this may seem beneficial to everyone because the government is able to leverage its SBIR funds with VC funds, the real issue is fairness. Most small businesses do not have access to VC funds. Therefore, outside money definitely gives an unfair advantage to the VC-funded small business such that one would expect more multiple wins of both Phase I and II grants by the VC-funded company.

It for these reasons we oppose any changes to the SBIR program that will permit VC-funded small businesses or small businesses under control by a large business and/or a VC firm from being eligible to participate.

Sincerely yours,



Dr. Wayne D. Kimura
Vice President of Research and Development